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The ECONOMIC DIGEST

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ECONOMIC RESEARCH COUNCIL

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The

ECONOMIC DIGEST

JULY 1950 VOLUME III NUMBER SEVEN

Joint Editors: Sir Geoffrey Bracken K.C.I.E., C.S.I., H. S. Goodwin

SEEN IN PERSPECTIVE

Over-Production Again?

PROBLEMS IN CONTROL OF SURPLUSES

By GRAEME DORRANCE

THE post-war years have seen a vast extension of bulk-buying and long-term contracts, primarily intended to protect the interests of consumers in a world of shortages.

Are we now in danger of re-creating once again the Frankenstein of "burdensome surpluses"? There are signs that in the production of tin, cotton and rubber supplies are already outrunning consumption; it is suggested in certain political as well as business circles that we will shortly be faced with serious over-production of iron and steel. Producers in many parts of the world still have vivid memories of the depression caused by the low level of basic commodity prices during the years before 1938.

Is there any sound evidence today that indicates a likely recurrence of the 1929-39 decline in prices? And even if such fears have a reasonable grounding, should we at this stage lay the foundations for regulation?

Even if one accepts signs of excess production at current prices, the situation in 1950 is radically different from that of the 1930s. After allowing for "normal" world price increases of more than 100 per cent, the London and Cambridge Economic Service estimates that the prices of many commodities, including sugar, cocoa, cotton, wool, jute and sisal, are well above any level that could be considered "normal." In their list of products reviewed, only tea, rubber, copper and tin appear to be "cheap," and the smallest price increase here is 125 per cent in terms of sterling. On the other hand the price of rubber is now so high that it may encourage further expansion of synthetic production. And a price of almost £600 per ton for tin does not appear to be "uneconomic."

However, there are problems today in certain commodity lines that suggest the need for regulation; already several schemes are being considered. On a small scale the British Government and the West Indies are negotiating a long-term sugar agreement, based on import and export quotas. The West Indians appear to be disappointed because Britain does not seem willing to guarantee a price almost at today's levels for the *entire* West Indian quota during the years 1953-

58. It is perhaps unfortunate that the West Indies did not take part in the 1931-35 Chadbourne sugar arrangements. Cuba, Java, Germany, Poland, Czechoslovakia, Hungary and Belgium tried to maintain a high price for sugar; the result was that their export sales fell from 12 million to 6 million tons, while the exports of their competitors rose from 15 million to 19 million. Naturally there was difficulty in reviving the scheme. It is interesting to remember that the Colonial Office had already made a similar attempt to maintain the price of rubber from 1920 to 1927; the result was a fall in British Empire production from 72 per cent. of the world total to 52 per cent.

Any arrangement between a limited group of countries is likely to bear the seeds of trouble. Even assuming that all producers can be brought into a scheme, tremendous difficulties arise when an attempt is made to supplant the market mechanism. One of the major operations of a market is to equate total supply with total demand. Producers will support plans which circumvent markets only if they can see a net gain in the form of an increase or at least a reasonable stability in price levels. Where high levels of demand are today being satisfied, the continuation of production at the present rate would lead to the accumulation of surpluses, a policy that can hardly be defended. For when and where could the surpluses be disposed of?

Yet production limitation is notoriously difficult to undertake. Unless production is to be determined by specific ordinance—and in many parts of the world such ordinances simply cannot be considered enforceable—taxation is the only possible method of control. Such a policy is almost bound to be subject sooner or later to the stricture that it "depresses the standard of living." The existing Uganda cotton scheme is already facing this difficulty.

Moreover fiscal methods are tricky to apply: in 1935 the Indonesian authorities found an export tax of 29 cents per kilogram on rubber ineffective in restricting output when the price to the native producers, before deduction of tax, was only 33½ cents.

Assuming that restriction of production is to be enforced—what can replace the market mechanism as a determinant of uneconomic production? Should this function be delegated to a committee of government nominees, who are bound to have in mind many matters extraneous to the situation under immediate consideration? The National Coal Board's recent experience in trying to close inefficient mines is instructive on this aspect.

Should this function then be delegated to a board of independent experts with power to allocate and (perhaps more important) enforce production quotas within the territories of independent countries? Granted that allocation could fairly, and agreeably, be decided the question of determining exactly how production is to be restricted still has to be faced. Previous restriction schemes have encountered serious difficulties because individual producers have been able to expand production without bearing many of the costs which have been imposed on those producers subject to res-

1. *ECONOMIST*, *March 25, 1950, p. 664 gives evidence of over-production referred to in paragraph 2, page 289 above.*
2. *C. F. Carter, "World Commodity Survey," Bulletin of the London and Cambridge Economic Service, May, 1949, p. 63 gives statistics showing various price levels of commodities referred to in this essay. The classifications used are based on figures in Bulletin, May, 1950, p. 135.*

triction. This was probably true of the pre-1938 rubber scheme. It is becoming more obvious every day that one cannot forget costs entirely, or be completely willing to follow the lead of one of the leading supporters of the proposed new tin arrangement who claims that "low cost production is itself inefficient."

We have mentioned only a few of the difficulties that must be faced if any attempts are to be made to regulate commodity markets during the next few years. They are not insurmountable.

An indication of what may be expected can be seen in the sliding price arrangements under the Internation Wheat Agreement. But many other approaches will have to be explored. Conditions are developing which will make market regulation and supply control as attractive to many producers as they have been over the past few years to consumer interests. If the interests of both producers and consumers are to be protected, research and the negotiation of agreements must needs be taken slowly and with great care.

SALIENT FIGURES OF THE MONTH

		Latest Month	Increase (+) or Decrease (−) on a Month Ago	Increase (+) or Decrease (−) on a Year Ago
"BUSINESS" INDICES				
Production		* 132.0	+ 1.0	+ 9.2
Purchasing Power		* 106.6	− 0.4	+ 0.3
MANPOWER				
Total manufacturing industries ...	thousands	*8,402	− 14	+177
Cotton spinning and weaving ...	do.	* 329.8	− 1.3	+ 8.2
Coal (on colliery books)	do.	702	− 2	−24
Reg. unemployed (G.B.)	do.	329.0	− 18.3	+ 4.1
PRODUCTION				
Index of production	(1946=100)	* 143	+ 3	+19
Coal (average weekly output)	(thousand tons)	*3,982	−405	+24
Steel ingots and castings (do.) ...	do.	324	− 6	+19
Cotton yarn (do.)	(million lbs.)	* 19.0	Same	+ 1.1
Woven wool fabrics (do.)	(million linear yards)	* 41.73	+ 4.58	+ 9.97
Passenger cars (do.)	(thousands)	9.58	− 0.62	+ 2.44
Commercial vehicles (do.)	do.	5.05	− 0.22	+ 1.32
Permanent houses completed ...	do.	14.86	− 4.53	− 0.25
TRADE				
Value of imports	(£ millions)	211.0	− 10.3	+23.5
Value of exports	do.	156.0	− 28.4	+18.6
Freight train traffic	(million tons)	5.25	− 0.45	+ 0.09
Retail sales	(1947=100)	* 133	11	+14
FINANCE				
Currency in circulation	(£ million)	1,258	+ 17	− 2
Deposits in London Clearing Banks	do.	5,843	+ 60	−43
Provincial cheque clearings (av. working day)	do.	6.68	+ 0.53	+ 0.50
WAGES AND PRICES				
Weekly wage rates	(1947=100)	110	Same	+ 2
Retail prices	(1947=100)	114	+ 1	+ 5
Wholesale prices	(1930=100)	† 254.5	+ 4.8	+21.2
Basic materials	do.	† 348.0	+ 14.0	+48.2
Intermediate	do.	† 282.6	+ 4.7	+23.0
Manufactures	do.	† 230.1	+ 1.7	+ 6.0
Import prices	(1938=100)	131	+ 3	+15
Export prices	do.	118	Same	+ 6

* March. † May. All other figures refer to April.

Schuman-Monnet Food Plan Coming

By MICHAEL HOFFMAN

According to this well-known Geneva correspondent of the New York Times, the Schuman-Monnet steel plan for Europe will be followed by a similar plan for pooling agricultural produce

IF Britain decides to participate in the proposed French-German steel and coal combine, an even more fundamental measure of integration of the Western European economies will be sought.

This would involve a pooling of French-British agricultural resources parallel with the pooling of coal resources. In such a programme the principal element of immediate importance would be French assumption of responsibility for furnishing Britain with a large percentage of meat supplies and the eventual creation of one unified market for nearly all agricultural products.

M. Schuman

Dicussion of this project actually pre-dates by many months serious discussion of the coal and steel merger. Sir Edwin Plowden, chief of Britain's Central Economic Planning Staff, and Jean Monnet, head of the French Planning Commission, and members of their staffs have been prime movers in this new approach to the integration problem. M. Monnet is mainly responsible for putting across Foreign Minister Robert Schuman's steel and coal proposal in the French Government, acting on the same line of thought.

Sense of Insecurity

The essence of this approach is to attack the causes of economic nationalism instead of its symptoms and to avoid trying to attack all the causes at once. M. Monnet believes that a main reason for the unsatisfactory progress toward a better integrated economy is the deep sense of insecurity, both economic and military, throughout Western Europe. Britain is more influenced by a feeling of economic insecurity and France more by a feeling of military insecurity.

Britain is preoccupied with the implications of the fact that somehow her island population must be

From the New York Times, May 10, 1950

fed, and, unable longer to control the overseas resources from which most of that food must come, tends to hoard every bit of bargaining power she can muster as a means of insuring those food supplies. Britain does not and cannot, in the present circumstances, rely on anybody else's feeling responsible for feeding the British people.

France, on the other hand, has always felt it necessary to conserve and improve all resources possible to keep up her military potential. If French steel output is not high enough to guarantee military needs, nobody will step in to fill the gap as a matter of responsibility rather than as a matter of goodwill or commercial gain.

Common Responsibility

M. Monnet believes these traditional viewpoints to be obsolete. The problem is to make the governments and the people realise that they are obsolete and start acting on the more realistic assumptions of common responsibility—to which lip service is paid but which is not the basis of governmental action.

The proposal for a French coal and steel merger with Germany is the first effort in Western Europe to establish common responsibility in an important industrial field. The next big break with the past that those who believe in the new approach would like to see is the establishment of a common French-British responsibility for feeding the French and British people.

This, too, could be extended to include other countries, notably the Netherlands, Belgium, Denmark and Germany. It is M. Monnet's thesis that the agricultural policy in Britain and France should be based on the assumption that the British people can consider French food resources as their own, and the French farmers can consider the British market as their own.

M. Monnet

The implementation of any decision to merge agricultural resources would bristle with difficulties. Neither country could go the whole way to a unified farm market at once because of deeply entrenched protected interests.

But there are also favourable factors. One of these is the growing concern in Britain about the cost of highly protected agriculture under present policies adopted in an effort to reduce dependence on overseas, particularly dollar food. Another is the adaptability that the French meat industry has shown in meeting British requirements under the current experimental contracts.

Arresting Points from Survey of Europe 1949

From an important report, vast in volume and scope, the following six points have been selected because they are specially quotable or debatable or significant for the future

(1) IMPACT OF LIBERALIZED ECONOMIES ON FULL EMPLOYMENT

In economies based on private enterprise, detailed controls in the sphere of production and trade often have the incidental effect of increasing real costs, directly through the manpower absorbed in the controlling machinery, and indirectly by thwarting technical progress and rationalisation. Allocations of raw materials, for example, are usually based on the individual firm's performance in some base period, so that efficient firms are held back from expanding, while inefficient firms are kept alive.

While the removal of physical controls over private business may contribute to higher efficiency, it is less certain that it means a return to the same degree of competition in the economy as existed before the war. The widespread system of government controls has been administered in close co-operation between government departments and trade associations whose collaboration was called for in establishing procedures for the distribution of licences, etc.

Trade associations thus acquired new functions; and where they did not already exist they were often formed in order to protect the interest of the trade *vis-a-vis* the controlling authorities, a development which was often fostered by the authorities themselves in order to ensure that the various controls would function smoothly in practice. The discontinuance of government controls does not mean that the co-operation between the members of trade associations will also come to an end.

Much of this co-operation serves useful purposes, such as the collection of statistics, the dissemination of technical information, and the promotion of exports; but in many trades it may also take the form of private price agreements to restrict the entry of new firms into the trade.

The trend towards abolition of controls brings to the fore the question of control over monopoly prices and other restrictive practices.

In countries where the internal economy has been largely liberalized, the maintenance of employment is precarious, depending as it does on a dexterous adaptation of monetary and financial policy to changing circumstances. Post-war experience is as yet insufficient to provide a clear answer to the question whether full employment can be steadily maintained under a liberalistic economic policy.

The conflict between the maintenance of internal stability and full employment and the desire for the

From Economic Survey of Europe in 1949, Economic Commission for Europe, Geneva, May, 1950.

abolition of controls is likely to continue to be a main issue of economic policy.

(2) TRADE LIBERALIZATION OBSTACLES

It is difficult to see how the benefits of a balanced and relatively free trade can be enjoyed, even among countries outside the dollar area, unless a closer and less restrictive balance with the dollar area is restored or adequate and continuing means of dollar financing are in sight.

Given that western Europe is not, and may not quickly become, a closely integrated economic and political entity, trade among western Europe countries cannot be insulated from the influence of trade with other countries. The longer-run objectives sought under the trade liberalization programme are thus dependent on attainment in the shorter term, of the viability sought under the European Recovery Programme as a whole.

This is a world-wide problem rather than a European problem. The risk is that, if the wider problem is not solved, inability to attain the objectives established within its intra-European aspects may result in disillusionment and impair the mutual confidence on which sound international trade relations must be built.

(3) CAPITAL TRANSFERS TO OVERSEAS AND DOLLAR DEMAND

Capital transfers from European countries to overseas countries of the same monetary area are commonly thought of as giving rise to no balance-of-payments burden, since direct conversion of funds into hard currencies is not involved. (Part of the illicit movement of European capital into dollars has occurred, of course, via leaks in the foreign exchange control systems of affiliated overseas countries.)

There are, however, several ways in which such capital movements, as well as releases from previously accumulated balances in sterling or other European currencies, may place an additional strain on European resources of goods and of foreign exchange:

(i) Capital transfers to overseas areas tend to support demand for European goods and to encourage exports to these soft-currency areas to the possible detriment of exports to hard-currency areas.

(ii) The total level of demand in overseas areas may be increased, both by the direct effect on domestic buying-power in local currencies and by the increase in the total exchange availabilities of the overseas areas. If these additional funds had not been available, or had been available in lesser amounts, the total imports of overseas countries affiliated with European currencies would necessarily have been held more in line with their current export receipts.

This might have meant not only a smaller volume of imports from European sources, but also a smaller demand for imports from the United States, and, hence, for dollar exchange out of the central reserve holdings. The overseas areas in question might thus have been brought nearer to the pre-war position, when they were normally net earners of dollars on current account with the United States and also made settlements to Europe in currently produced gold.

(Many of these overseas countries however—notably India and Paki-

stan—have themselves experienced severe economic difficulties during and after the war, and their problems would have been more serious if they had not been able to draw on their holdings of European currencies.)

Dollar outlays have been small, however, in two of the overseas countries to which private capital has moved in large amounts. In Australia, to which a considerable part of the private capital movement from the United Kingdom has been directed, it has so far led chiefly to the accumulation of idle sterling funds in London to the credit of Australia. Australian imports from North America have actually been smaller in volume than before the war, although rising substantially from 1948 to 1949.

In the Union of South Africa, capital transfers from the United Kingdom contributed towards the building up of an extremely heavy import demand in 1948, but the dollar deficit was met through the Union's own gold resources. A recent agreement with the United Kingdom stipulates that payment will be made in gold for certain types of essential goods. This provides the United Kingdom with an opportunity to earn gold in that market even though its export surplus may be more than offset by capital movements.

(4) INEFFICIENCY OF EXCHANGE CONTROL

Experience suggests that, when the political and economic prerequisites of stability and confidence are lacking, exchange controls and payments agreements, however cleverly contrived, prove seriously inadequate to prevent the flight of private funds on a scale sufficient to impose intolerable burdens on official currency reserves.

On the other hand the return of private capital from its places of hiding at home and abroad is capable of providing large and otherwise inexplicable additions to available exchange resources. To take a recent example, there seems little doubt that the re-emergence of hoarded funds contributed substantially to the strengthening of the French franc during the past year.

If Europe's political and economic development is favourable during the next several years, the cessation of losses through the exodus of private capital and the possible repatriation of part of the funds previously transferred abroad could lend further vigour to recovery.

If, however, European countries find themselves with slender reserves and persistent difficulty in covering their dollar payments, uncontrolled private capital transfers could turn a bad situation into financial and economic disaster.

(5) BRITAIN'S SPECIAL ROLE IN OVERSEAS TRADE

Most European countries continue to have large deficits in their dollar accounts, and each of them will have to make adjustments in order to achieve equilibrium, but the problem is largely centred in the position of the United Kingdom.

Because of its readier access to sources of supply within the overseas sterling area, the United Kingdom has been in a better position than other European countries to economize in its own direct dollar outlay on imports from the United States. Nevertheless, it has had to make extremely heavy dollar settlements and other dollar transfers to

many other overseas areas, despite the large increases achieved in its overseas exports and the severe restriction of its imports.

This has resulted partly from the change in its international position since the war, especially the fall in its net earnings from overseas investments and the far greater reduction in their effective buying power at current prices. A still more important cause, however, lies in the change in its position at the centre of a major monetary and economic area from which it no longer received the gold and dollar settlements that played an essential role before the war in financing the United Kingdom's import surplus from North America, as well as from Continental Europe.

As a consequence of the change in the United Kingdom's position, other European countries have been unable since the war to rely on financing their overseas imports through earning surpluses in trade with the United Kingdom, and it appears doubtful that they will be able to do so again, at least for a number of years to come. These countries have thus become more directly confronted with the dollar problem in their relations with the United States, but there is little evidence that any of them have yet been able to make the adjustments that are required by this change in the pattern of payments.

The increased dependence on the United States, both for imports and for dollar financing, is most pronounced in western Germany. The problem is aggravated there by the increase in the general level of import requirements, resulting from the breakdown in inter-zonal trade and from the extraordinary postwar increase in population, and by the limited recovery of its exports, especially in trade with overseas areas. The low level of German exports has been especially marked in Latin America. This in turn has increased the demand of these markets for imports from the United States, thus enlarging the scope of the dollar problem.

With the re-emergence of German competition, in European as well as in overseas markets, the burden of the dollar problem may be shifted in some measure from one country to another.

For countries historically dependent on Germany as a source of supply for manufactures and as a market for their own products, the burden may be lightened. But in other countries, and principally in the United Kingdom, the competition may be felt both in bidding for available supplies of foodstuffs and raw materials, and in selling capital equipment and other manufactures. The recovery of Japanese trade will also tend to increase the competition that Europe faces, particularly in exports of textiles and other consumers' goods and in imports of textile fibres and other industrial materials.

Can the United Kingdom and other European countries adapt themselves successfully to these new competitive forces? Can continental European countries make the adjustments demanded by the change in their relations with the United Kingdom? The answers largely depend on whether or not there is a sustained expansion of world production and trade.

(6) PENALTIES OF STALEMATE IN EAST-WEST TRADE

It is important to understand the economic consequences of the stalemate in east-west trade. For

eastern European countries—particularly the smaller eastern countries which are historically dependent on manufactures from western Europe—the failure to obtain capital goods and other manufactures from the outside, even in the limited volume imported before the war, can only mean increased difficulties and delays in the attainment of their industrialization objectives.

However impressive the relative increase in intra-eastern European trade has been, the supply of capital equipment that can be obtained from within the area is probably extremely small in relation to their industrialization objectives.

For western Europe the question is primarily that of the balance of payments or, more specifically, the need to find markets which can both absorb exports of manufactures and supply foodstuffs and raw materials. The failure of east-west trade to recover intensifies the problem, which reaches its more acute stage in the present structure of German trade.

Long Term Policy for Europe

By

M. MARJOLIN

Secretary General O.E.E.C.

The recent Economic Survey of Europe (dealt with in the previous article) complained of lack of policy for Europe after 1952. The Organization for European Economic Co-operation is trying to supply what was lacking

THE need for a long-term programme has been explained to the O.E.E.C. Council by the Secretary General, M. Marjolin. He pointed out that the Organisation is now starting the preparations for its third annual report, to be published at the end of this year.

This report will be of special importance. In 1951, President Truman will ask Congress for the last instalment of Marshall Aid. He will necessarily have to state Europe's prospects for the years following the termination of such aid. Mr. Gordon Gray has already been asked to examine the question of world economic equilibrium after 1952.

In order to co-operate usefully with the Americans, Europe must also assess the future at this stage. M. Marjolin, therefore, proposed and the Council agreed that each country should give details of its own proposed objectives for the next four or five years. It should endeavour to lay down the main lines of its investment programme together with its intended policy to

From The Statist, London, June 10, 1950.

ensure the greatest possible development while preserving internal financial stability.

The role of the Organisation will be to compare the national objectives and to harmonize them so as to avoid contradictions and waste of resources. Any difficulties encountered by individual countries will be examined and the greatest possible joint effort will be made to overcome them. Lastly, the Council at ministerial level will examine, two or three times a year, a report on the progress achieved by member countries in their efforts to reach viability. The detailed plan of work will be prepared by O.E.E.C.'s executive committee.

In the course of his statement, M. Marjolin stressed that future action must be based on a "clear view of the problems over a sufficiently long period." The conclusions to be reached should "fit into a more comprehensive perspective. . . . . . European problems are inseparable from those of the whole Western world and, in particular, the dollar shortage must be dealt with on a world scale."

As in 1947, a plan of action is required now. In spite of much progress, even on the most favourable assumptions, the position in 1952 will be "precarious and unsatisfactory." In addition, it will only be possible to "restore the social and economic balance of the free world if the development of economically backward areas proceeds rapidly."

If Europe wishes to maintain its world position, it must take part in the enterprise of President Truman's Point IV and "make available large quantities of capital equipment and consumer goods within the compass of its resources." Joint action by the member countries will be necessary to overcome difficulties, especially in the internal and external financing of such a policy, but "each member must be free to choose its own line of approach to the objectives jointly agreed."

The closest co-operation with the U.S. and Canada should be used as a means to integrate the economic expansion in Europe in the development of world economy. Rapid expansion of Europe's economy is necessary if such objectives as the progressive liberalization of trade and a greater freedom of movement for workers are to be attained.

BENELUX

A statement by the Dutch Minister of Finance, Professor Lieftinck, shows that within the Benelux partnership great problems remain unsolved. Towards the end of 1949 trading increased greatly, but every month showed a more noticeable deficiency in Holland's balance. At the end of November the deficit amounted to 12 million guilders; at the end of December to 30 million guilders; in January, 1950, it grew to 42.5 million guilders; in February to 66 million guilders; in March to 78 million guilders, and in April to 84 million guilders. It is doubtful whether these deficits will be coverable by drawing-rights and credits, the report indicates. The trend will remain in the direction of growing Netherlands deficits, and is likely to be accentuated by the formation of the Economic Union.

Statist, London, June 3, 1950.

Whose Headache is the Dollar Problem?

By MARRINER S. ECCLES
Member of Board of Governors of U.S. Federal Reserve System

MR. ECCLES sees three problems on the American side. The first is summarized by the clear inconsistency which characterizes present U.S. economic policy, viz. preaching the doctrine of free economy in the international field and following at home practices which completely contradict the very concept of a free economy.

The second is the collision between the desire to increase imports to close the dollar gap, and the desire to avoid serious inconvenience to any part of the U.S. domestic economy that might result from increasing imports.

The third dilemma is presented by the desire to maintain markets for U.S. exports, and the desire to keep down imports and bring U.S. foreign aid to a speedy end.

As examples of inconsistencies in U.S. general policy Mr. Eccles cites U.S. import prohibitions and import quotas for a number of agricultural products, high tariffs on particular industrial goods and the provision that repairs on American ships carried out abroad shall be taxed at the rate of 50 per cent. unless proved as urgent.

In addition, there is a philosophy which perverts the meaning of " full employment " and makes it mean a guarantee that " all firms now in existence and every worker employed by those firms must be kept doing what they are now doing." This leads to demands to prop up the " victims " of free economy; it leads to the programme of agricultural support prices and to the toleration of the growth of labour monopolies.

As to closing the dollar gap through a rapid increase of imports into the U.S. by means of abolition of tariffs and quotas, Mr. Eccles accepts the calculations that the total volume of such imports would be so small compared with total U.S. production that there need be no serious concern about the resulting disturbances for the American economy " taken as a whole."

Death of Industries

Nevertheless, he does not think that such calculations prove that no dilemma of national policy is involved. These imports might be concentrated within such narrow sectors that the result could be the death of industries which, though small, represent the means of livelihood of a majority in specific localities (examples: shoes, textiles, watches, pottery).

If, however, U.S. producers, no matter how small their aggregate contribution to the total national product, are to be protected against foreign competition, and foreign aid is really brought to an abrupt end in 1952, then the effect will be a catastrophic narrowing of the U.S. export markets in wheat, maize, cotton, tobacco, fats, oils, industrial

From United Nations' World Magazine, May, 1950.

raw materials and machinery even where the U.S. offers a clear price advantage.

U.S. Would Suffer

This would put the full burden of adjustment, in the form of unemployment and loss of invested capital, on the present export industries. Such a destruction of U.S. exports would not only hurt the U.S., but also her allies, to whom the loss of their export markets would mean not only unemployment but also deterioration of living standards.

There can be little doubt, Mr. Eccles continues, that Britain has been able to extend economic and military aid to our other allies only because America has been willing to provide Britain with dollars, partly in payment for her exports to us and partly in the form of direct aid. If we cease to provide dollars for Britain in either of these two ways, we shall at once have to provide aid to the other Allies which so far have obtained aid from Britain. Thus the dollar burden of the American taxpayer would not be reduced.

There are no magic solutions. Such solutions as have been discussed are not completely wrong, but one-sided. Their weakness is in failure to strike a balance between the need for adjustment and the need for finding ways to adapt the pace of adjustment to the realities of economic and political life. A middle line of policy should be worked out, one which will cause a minimum of dislocation of the American economy while the long-term aims are pursued.

To refrain from setting up new barriers will cause less dislocation than would insistence on a sharp and sudden reduction of existing barriers to imports. To accept a gradual decline in the share of U.S. exports in world trade will cause less dislocation than would a sudden contraction of those exports as a result of new import restrictions or the sudden cessation of foreign aid.

In the meantime long-run factors will help to ease adjustment. Increase of population and *per capita* income, in combination with the depletion of American natural resources (e.g. iron ore, copper, timber, oil) will create an increased demand that will enable the U.S. to buy abroad without injury to domestic producers. Finally, the whole picture of world trade will improve as progress is made toward ending the cold war.

It is a question of "buying time" within which long-run forces can help us along the right road. If the price of " time " that we shall thus be buying is to be the maintenance of our tax burdens for a longer period than some had hoped, Mr. Eccles concludes, we should remember that there is no solution of the dollar dilemma which will be without its price in dollars.

THE ETERNAL TRIANGLE

Since the British authorities negotiated agreements to prevent " triangular " sterling transactions being undertaken by transferable account countries, a new technique has developed. Import contracts labelled in sterling for these countries are being switched over in many cases into national currencies. By this means the former " triangular " transactions are conducted in the national currencies but as long as the Bank of England is purchasing these currencies, the transactions will have much the same effect as the previous " triangular " transactions over sterling.

Economic Bulletin, National Bank of Egypt, Cairo. Vol. III., No. 1, 1950.

National Income as Policy-Makers Guide

By RICHARD RUGGLES
and J. R. N. STONE

National income accounting is a matter of growing importance in domestic and international affairs. Some of its values — and some of the traps in the path of the unwary — are here explained

ALTHOUGH national income accounting is by itself in no sense a sufficient basis for formulating economic policy, it is of use in helping to answer certain questions about overall economic policies. These questions, specifically, are of three major types:

1. Is the policy which is being considered capable of being achieved in terms of the availability of resources?

2. How does the policy affect the operation of the economy in terms of prices, output, and employment?

3. What is the net effect of the policy in quantitative terms? Is it worth doing?

Each of these questions will be examined in turn.

(1) *Economic policy and the availability of resources.* It might seem that almost any policy which advocates increased output somewhere in the economy is basically a good policy, since increased goods and services are a desirable goal. But, when the problem is considered in the context of the potentially usable resources in the economy, it is apparent that advocating an increase in one particular industry is tantamount to declaring that it will be more beneficial to use additional resources in this industry than in any other industry.

For a valid defence of the policy, it would be necessary to show what additional resources would be needed to carry it out, from what part of the economy such resources could be obtained, and why this particular use would be more beneficial than alternative use of these same resources in other industries.

For all of these questions, the information available in the national income accounts is pertinent. The quantity of additional resources needed to carry out an economic policy cannot be computed without regard to inter-industry relationships. Should an increase in naval construction be proposed it is not enough to consider the increased manpower required for actual construction. The manpower and facilities involved in the components industry, in the steel industry, in coal mining, and even in industries as far removed as chemicals and electric power must also be considered.

With a knowledge of the general requirements of the programme, the national income accounts show the relative expansion in the output of these industries, or the contraction in the use of their products by other industries, which would be

From National Income Accounting and Its Relation to Economic Policy, Economic Co-operation Administration, Paris.

needed to carry the programme forward.

Alternatives to the proposed policy should also be considered in a similar manner—for instance, in this case it would be useful to study the cost, in terms of economic dislocation of air fleets. The usual comparison in money cost terms alone is not enough. Some parts of the economy cannot easily expand further, whereas other parts may actually be operating below capacity. To insure the fullest possible utilization of resources such factors as these should be taken into account, and the final economic policy which is recommended should be based on the explicit belief that it is superior to all possible alternatives.

Second Group

A second major group of economic policies are those which refer to the economy as a whole and are quite general in their coverage. An economic policy of this type is only meaningful if it fits within the limits of the existing resources on the economy, and if it is internally consistent. The production of food will not increase at the same rate as the production of steel or even textiles. The rate at which different industries grow is governed by the manner in which the consumer spends his income, the kinds of goods and services which are purchased by the government, and the nature and level of the capital goods industries.

Further differences in rates of growth are introduced by technological factors; the ability to utilize mass production permits some industries to operate at decreasing cost, whereas the limitation of available resources prevents expansion in others. Inventions and changes in technology also complicate the situation for almost all industries.

Because of these complexities met in analyzing overall economic growth, the governments of most countries in which national accounts are available use these accounts to make projections of the effects they believe their economic policies will have. These projections are frequently referred to as "national budgets"; in effect they show the change that is to be expected in each part of the economy.

Since these projections of the national accounts are usually presented in terms of constant prices, the separate accounts will only balance and tie in with each other if the net increase in output does not exceed the assumed change in available resources. The making of the projection therefore insures that the projected changes will be within the expected potential limits of the resources.

Superior Results

Using the national accounting system to integrate the effects of an overall economic policy with the economy as it exists and as it is expected to change in the future, it becomes possible to see whether the proposed economic policy is consistent with itself and whether it can be expected to produce a result superior to those of alternative general economic policies.

(2) *Economic policy and the operation of the economy.* Badly designed economic policies can result in serious inflations or depressions, so that it is necessary to give careful consideration to the relation of any proposed policy to the actual functioning of the different sectors of the economy. An

example will demonstrate the use of national accounts for this purpose.

Consider a proposal to reduce the public debt. Suppose that the actual mechanism proposed is increased taxation of individual incomes in order to obtain a government surplus to be used for debt repayment. Further let it be assumed, for the sake of concreteness, that most of the debt repayments would be to banks holding government bonds. Making use of the sector accounts, it is possible to trace through the effects of both the increase in taxation and the debt repayment.

Personal Taxes

On the personal income and expenditures account, the amount of personal taxes paid would increase, and individuals would be forced to curtail their personal savings or their consumers' expenditures. Since every entry appearing on the account of one sector also appears on another account in the economy, it is necessary to look at the other accounts to see how they will adjust to the changes in consumers' expenditures.

In the national allocations and expenditures account, consumers' expenditures must be reduced by the same amount that these expenditures were reduced in the personal income account. This of course means that the total for all expenditures (i.e., gross national product at market prices) must also be reduced, and it follows that if the account is to balance the allocations will have to change simultaneously.

In all probability, as a result of the decline in consumers' expenditures producers will receive fewer orders, and they will therefore cut back production, causing some unemployment. The decrease in wages and salaries in turn must be entered on the personal income account, as a decline in personal income. Individuals will undoubtedly react to this decline in their incomes by cutting their expenditures again, and again producers will sell less and so be forced to dismiss more workers, increasing unemployment. Debt repayment to the banks will not necessarily help the situation. The debt repayment represents a current payment by the government, but it does not represent a current payment *of income* to anyone in the economy. There is no reason to believe that producers will borrow to expand their investment expenditures merely because the banks now have cash instead of bonds. The more probable development is that with the initial declines in consumers' expenditures and in output and employment, producers will curtail their investment expenditures, so leading to an even sharper decline in gross national product, output, and unemployment. The use of national income accounting thus reveals that this economic policy designed in this particular way, on the surface apparently desirable, might actually have disastrous results.

Equalized Incomes

Just as a badly designed economic policy can cause a depression, so it can also result in an inflation. Suppose for example that the government, although it desired to keep the budget balanced, decides to equalize incomes somewhat by removing some of the taxes from the lower income groups and placing equivalent taxes on the upper income groups.

The immediate results of this action would appear on the personal income account as a rise in consumers' expenditures and a fall in personal saving. The lower income groups would be given larger incomes to dispose of by the tax reduction, and they would undoubtedly react by spending most of the additional money which became available to them. On the other hand, the people of the upper income groups who were now paying more taxes would have to reduce their savings in order to be able to meet the increased taxes and still maintain approximately the same standard of living.

Rise in Prices

In terms of the national allocations and expenditures account, these reactions would appear as an increase in consumers' expenditures, and, if only a limited quantity of goods were available, the prices of consumers' goods would rise. Producers, because of the increase in consumers' expenditures, would have more money to allocate over the factors of production, and more would be available to meet labour's wage demands. Personal income would therefore increase, and consumers' expenditures would again rise, starting the spiral all over again. Producers' reactions to the higher level of activity in the economy would reinforce the spiral; they would increase their expenditures on capital goods and thus further increase the gross national product.

(3) *Economic policy and its quantitative effect*. The final question that must be considered is that of the actual results which an economic policy can be expected to achieve in terms of the goals of the society. National income accounting obviously can never give a complete answer to this question. The welfare of individuals cannot be measured in terms of a few summary measures. There are many non-quantitative ingredients—such things as working conditions, freedom of opportunity, and the moral and political temper of a country.

But national income accounting can and does shed some light on what is happening to the end uses of production. The calculations of the expected expenditures on the national allocations and expenditures account in terms of constant prices will show the quantitative change which is expected to occur in the goods and services available for specific end uses. This information, even though it is by no means a complete basis for evaluating any policy, is very much needed.

Degree of Risk

Policies which have a large degree of risk attached to a small possible gain are naturally excluded from any reasonable consideration. In like manner, the expected results of an economic policy need to be estimated in quantitative terms in order that the possibility of gain may be weighed against the risks of failure. Many policies which in theory are beneficial may be found, when examined in quantitative terms, to make so little difference that they are not worth undertaking.

Fair Start for Commonwealth Conference

THREE major programmes were discussed at the Sydney Conference of the Commonwealth Economic Committee. The first was a proposal to build up an emergency reserve of food supplies and drugs, intended to be distributed in Indonesia, Burma, Thailand and Viet-Nam. This was the immediate programme, which led to controversy at the conference.

The second was the short-term technical assistance programme, involving an outlay of £8 million in three years, and intended to finance the training of some 3,000 technicians from the South-East Asian region. The cost of this programme is apparently to be shared in the proportion of 70 per cent. by Australia and the United Kingdom, a little more than 10½ per cent. by India and a little less than 19½ per cent. by Canada, Pakistan, Ceylon, and New Zealand.

The provisional allocation of trainees reportedly contemplates that some 300 to 500 trainees will be received in India, and some 300 by the overseas dominions, the others being trained for the major part in the United Kingdom.

This part of the programme gives concrete shape to the American theory that know-how of an elementary kind, even if it is not completely adequate, will inevitably have to precede the expenditure of vast sums of money in this region.

The third programme discussed at Sydney was longer-term aid, spread over six years; and though a figure of £15 million has been mentioned for this purpose, the official communique itself merely calls for estimates by the 1st September, 1950. with every intention of discussing the matter further at London.

On a dispassionate view, the net results of the discussions were chiefly two. It was established at Sydney that economic development in areas which are not immediately threatened by Communist uprising or warfare is a matter of urgency. It has also become clearer that while outside help need not be ruled out—for the business community in the United States is, by and large, markedly in favour of aid to Asia on a large-scale—the immediate action has to be taken within the Commonwealth itself.

The sense of realism which prevailed at Colombo, and even more than the sense of realism, the Commonwealth's ability to act together, may prove to be valuable in future, if any programme of aid does materialise. Point-Four Aid has just had a modest start with 35 million dollars, while it is not beyond the bounds of possibility that that portion of the aid which is intended for South-East Asia may be distributed in consultation with the Commonwealth Economic Bureau.

Any additional allocation which may be voted hereafter, will almost certainly be spent after taking the Commonwealth's long-term plans. which will be co-ordinated at Colombo, into consideration. It is no secret that from the point of view of the United States, which is the only country today which is in a

From the Eastern Economist, New Delhi, May 26, 1950.

position to lend, a promise of effective economic co-operation, however modest, will be welcome.

This, however, is a hope which belongs very much to the future. The most valuable lesson to be learnt from the Sydney Conference is that while Commonwealth co-operation may in the end amount to something, there is no alternative immediately to national action. Political and economic liaison cannot be a substitute for action within the countries themselves to mobilise resources on a grand scale for investment.

Whether the saving required is 8½ per cent as the F.A.O. study estimates—having assumed liberal foreign aid—or whether it is more, there is no ready substitute for national policy which does not wait on international action. In the nineteenth century, and before the First World War, such a substitute was, perhaps, available. The grim rigour of the truth that there is no easy way out at present must have been adequately impressed on the delegates at Sydney, and, it is to be hoped, will be adequately communicated to their respective Governments.

India's "Real War Costs"

THE cost of the war to India is reckoned, at 1939-40 prices, to be Rs. 1,503 crores, or over £1,127 million. India's national income is estimated as having increased over the war years by 619 crores, and the balance of 883 crores is assumed to be due to decreased consumption, as net drafts on capital investment were very small.

Compared with analysis of war costs in other belligerent countries, it is reckoned that India made greater inroads into current consumption than any other country.

War finance from :—	Japan	U.S.	U.K.	Germany	India
Larger Output	41.0	100.0	40.0	44.0	41.1
Decreased Consumption ...	41.0	−17.0	24.0	18.0	58.8
Decreased Govt. Non-war Expenditure	−3.0	3.0	2.0	Nil	Nil
Drafts on Investment ...	21.0	14.0	34.0	38.0	0.1
	100.0	100.0	100.0	100.0	100.0

From the Eastern Economist, April 24, 1950.

INDUSTRIAL DISPUTES IN U.K.

In 1949 the aggregate loss in working time was lower than in any year since 1942. During the period 1914 to 1918 the average yearly number of days lost was about 5,360,000. In 1919 to 1921, the three years following the first world war, the yearly average was about 49,140,000. From 1922 to 1932 (omitting 1926, when 162,000,000 days were lost, mainly in the coal mining dispute and general strike), the average was about 7,560,000. In the 17 years 1933 to 1949 the yearly total of days lost ranged from 940,000 to 3,710,000, the average being about 1,890,000.

Ministry of Labour Gazette, May, 1950.

Labour's Reply to Prophets of Woe

By ANTHONY CROSLAND, M.P.
Fellow and Lecturer in Economics at Trinity College, Oxford

Is it true that economists have, on the whole, been Jeremiahs? And are the facts of to-day, and the promises of the future, proving them wrong?

THE whole object of the economic process, though you would never guess it to hear some economists talk, is the production of wealth, of the goods and services which go to make up our standard of life. The higher the output of goods, the higher our real incomes and the better off we are—provided always we are paying our way abroad. Even the financial editors could hardly dissent from that.

The production of wealth depends mainly on two things. The first, obviously, is the number of people who have jobs and are actually producing. The more people are employed, the greater our national wealth. We can see now that the most inefficient thing about our pre-war system, quite apart from the appalling social misery which it caused, was the large-scale unemployment we then had. It was madly and incredibly inefficient to leave these hundreds of thousands of men on the dole, year after year.

They themselves were poor enough, but the whole country was poorer too, by the lack of the goods which they might have been producing. What a contrast today! Out of every hundred insured workers, over ninety-eight are at work producing wealth. Before the war, even in the best years, it was only ninety; in an average year it was eighty-six; and in the worst years it sank as low as seventy-eight.

You are sometimes told that before the war nobody understood about how to cure unemployment, whereas today we have all read Keynes, and we all know about full employment, so there is nothing particularly creditable about maintaining it in Britain. Don't you believe it—not for an instant. Just look at what is happening abroad at this moment. Compared with Britain, where ninety-eight out of a hundred workers are actually working, in America you have ninety-three, in Belgium eighty-nine, and in western Germany eighty-eight.

Full Employment

This shows that full employment does not just happen as a gift from heaven. It needs planning for. And it does not just need Marshall Aid—plenty of countries have Marshall Aid and unemployment too: for instance, those western European countries that I have just mentioned. This fact of full employment is by far the most spectacular difference between post-war and pre-war Britain—and it represents an immeasurable gain in economic efficiency. The second thing which our output of wealth depends on is

From BBC broadcast, Home Service, June 2, 1950.

the amount that each employed person produces. There is no doubt at all that by 1939 Britain had lagged far behind America and Germany in this matter of productivity. People say now that high taxation and Government controls are a deterrent to efficient production; but look at our pre-war position—no controls, a vastly lower level of taxation, and yet productivity falling further and further behind America and Germany.

Increased Productivity

Today, despite high taxation, our productivity is rising fast—by 5½ per cent. in 1949—over double the pre-war rate. Now this is an interesting fact, which you would never guess from reading certain newspapers: that our output per man is rising far more rapidly than under the unplanned system of pre-war days. Nobody likes high taxation, but whatever else it has deterred, it has not prevented a much healthier level of productivity.

Since more people are at work, and each person is producing more, our total production must also be higher. And so it is. There is a lot of argument about how you should calculate production, and it all depends on what base-year you take; but there is no getting over the simple fact that our total production of wealth is much greater than in any pre-war year.

I claim that this position—higher employment plus higher productivity equals higher total output—means that our economy is in a healthier and more efficient state than it has ever been.

We defined an efficient economy as one which was producing at a very high level of output—provided it was paying its way abroad. Obviously we should not have a healthy economy, however high our output, if we were unable, year after year, to pay for our imports, so that we were sinking deeper and deeper into debt. So a healthy economy demands that we do not have a deficit on our foreign balance.

Here I must draw your attention to a fact which far too people have noticed. We now have, taking account of invisibles, a surplus in our foreign trade: counting invisibles, total exports are greater than total imports; we are more than paying our way abroad. Do you know when the last year was that we had a surplus like this? It was in 1935. And the year before that? 1930. So except for one solitary year, we have not had a surplus for two decades past—until now. Doesn't this really entitle us to claim that we have a healthier economy than before—full employment which we did not have then, higher productivity than we then had, and a better foreign balance than we have had for twenty years?

Fool's Paradise

However, the Jeremiahs still have one line of escape. The more honest and clever ones will usually admit the facts I have mentioned, and admit they constitute a great improvement. But then they say: 'you are living in a fool's paradise: you may be all right now, buoyed up by Marshall Aid, but you will be sunk when it ends in 1952.'

This is a serious argument. Everyone knows that, despite our overall trade surplus, we still, in common with the rest of the world, have a dollar problem. Everyone knows we still rely, like the rest of

western Europe, on Marshall Aid, which finishes in 1952. Is it true that we face disaster when that time comes? The answer is to get this in perspective. Our dollar deficit is now only a third as big as it was in 1947. This is a really large improvement; is it really absurd to think we can eliminate the remaining third by 1952?

Or look at it another way. Our Marshall Aid is now only half what it was two years ago. If we could survive its halving in two years, is it unreasonable to hope that we can survive the disappearance of the other half by 1952? And remember—Marshall Aid only represents 3 per cent. of our total national product.

Dollar Situation

Certainly the present indications are good. Our gold reserves are improving faster than anyone expected. Our dollar exports are picking up well, especially to Canada. Devaluation has made our prices perfectly competitive, and it is no longer unusual for us to win contracts in third markets against stiff American opposition. Above all, we are continually cutting down our dollar imports and switching to other sources of supply. Our dollar imports are now far smaller than they were a couple of years back. Every month we switch a bit more and become less dependent on the dollar area. Every month, therefore, the dollar problem becomes more manageable. One can never be complacent about the dollar business, because so many things lie outside our control. For instance, we can plan our own economy, but not the American; and if the Americans should have a slump, then we (and the rest of the world) would certainly feel the draught.

Prospects Fair

But I claim that our prospects of independence by 1952 are very fair: we have reduced our dollar deficit enormously over the last three years; we are becoming less dependent on the dollar area every month; and we have the best record in the matter of dollar exports and imports of any of the Marshall Aid countries. When you add this to the full employment, the higher productivity, the record exports, and the surplus in our overall foreign balance, it surely does add up to a picture of reasonable health and efficiency.

Then what on earth is it which makes the Jeremiahs go on wailing? With the more old-fashioned economists and financiers, it is a natural irritation at seeing a system work which runs directly counter to their pet *laisser-faire* theories; rather than amend the theories, they deny the facts. With others, who find themselves paying rather more surtax than they used to, it is a subconscious refusal to admit that if they themselves are worse off, things can possibly be going well.

(Note: Mr. Crosland's talk did not rank as a party political broadcast, perhaps because the "prophets of woe" are not all to be found on the Opposition benches or in the columns of the Opposition press. And it is certain that some of the pilloried "prophets" will recall that history justified Jeremiah.

Eds. E.D.).

Sweden Uncovers Electrical Cartel

THE first authentic information about post-war cartel agreements in Europe has been published by the Swedish Government after an investigation that occupied nearly two years' time of a ten-man committee.

In meters, cables and copper and copper wire, all vital components of the entire range of end products of the electrical industry, the investigation revealed the revival of international cartel arrangements to restrict competition. This happened as early as 1946, when Europe was labouring through a period of great shortage of nearly all electrical products.

The post-war cartel builders have learned to dress up their agreements to make them look like part of the welfare state. The agreement on copper products (without which the motor and generator factories could not operate) states that "The parties shall try to attain a high and stable level of employment and a satisfactory standard of living for everybody employed in the nonferrous metals industry and to give every part of the industry unrestricted access on the same conditions to world trade in these products."

To this high-sounding agreement belong three Belgian companies, one French national cartel grouping fifty companies, an organization of ten British companies representing 85 per cent of British nonferrous metals output, two British export companies controlling 100 per cent. of British exports, a group of three Swiss companies and the leading Swedish company. No German companies belonged in 1946, but some may have joined since.

The method of giving everybody "unrestricted access" to world markets is to divide such markets into two sections—the home market of cartel members and markets that have no members in the group.

In the markets of members no other member may sell below that member's price—the "member" being itself a cartel that sets national prices or has them set by Government machinery, which it usually controls. In other markets no member may sell below an agreed price list kept up to date by a permanent secretary.

From The New York Times, May 17, 1950.

MONOPOLY LEGISLATION

Monopoly Legislation will be the subject of an address by Mr. Graeme Dorrance which will be given to members of the Economic Research Council in the Angus Room, 55, Park Lane, W.1., at 8 o'clock on Wednesday, July 5th. Mr. Ian Mactaggart will preside.

Mr. Dorrance is a lecturer at the London School of Economics and Editorial Secretary of the London and Cambridge Economic Service. He is also well-known to readers of the Economic Digest as writer of the articles which appear each month under the heading "Seen in Perspective."

Non-members will be welcome at the lecture if they will tell the secretary of the Economic Research Council that they intend to be present. The address is 18, South Street, London, W.1., and telephone number GROsvenor 4581.

Fiscal Policy and Monetary Policy Must March in Step

By W. M. SCAMMELL
Lecturer in Economics, University College of North Wales, Bangor

Full employment cannot be achieved by the techniques of taxation alone: interest rates must also be used

FISCAL policy is now the main instrument of government for regulating the flow of incomes. It is still early to make any sweeping claims on its behalf, but already enough has been seen to indicate that, intelligently used, it is a powerful weapon. The moderate success which has attended Sir Stafford Cripps's policy of disinflation, and the recovery of the American economy from the mild recession of early 1949, both indicate how effective fiscal policy can be.

Yet we must temper our enthusiasm a little. The world economy of 1950 is very different from that of the 'thirties. To the United States economy Marshall Aid, and to the European economies deferred demand, capital arrears, and shortages of consumer goods, have all served to keep demand and activity at ultra-high levels.

It must be remembered that between 1933 and 1939 President Roosevelt increased the National Debt of the United States by 24,000 million dollars without bringing the economy within sight of full employment. Certainly in the next ten years we shall have to fight hard to maintain the steady employment of 97 per cent. of the labour force, which is generally recognized as full employment; and, with the struggle impending, we should do well to examine carefully the weapons we intend to use.

Only a small minority would now wish to return to the use of monetary policy—bank rate changes and credit restriction—as the major instrument of overall control. But there are many who wish to see monetary policy used in a subsidiary role and as an adjunct to fiscal policy. It is argued that, by a successful marriage of the two, complete control of both income-flow and monetary supply would be achieved; private investment would be influenced by the relation of the interest rate to marginal efficiencies of capital, and certain of the direct quantitative controls on capital expansion might be dispensed with. It is worth while examing this problem.

Simple Recipe

Government policy since the war has relied on budgetary weapons backed up by direct controls, and no attempt has been made to use monetary policy. The recipe has been simple: let bilateral agreements and rigid exchange control govern the foreign situation, and let budgetary manipulation and con-

From The Changing Aims of Fiscal Policy, Westminster Bank Review, London, May, 1950.

trol of capital outlays govern the domestic.

But even a glance at the published figures of the clearing banks is sufficient to show that, throughout the last five years, monetary trends and fiscal policy have been at variance. During the chancellorship of Dr. Dalton monetary expansion was blithely permitted, side by side with heavy Government expenditure and investment programmes. The credit pump was continually primed by great increases in the amount of purchasing power. Between December 1945 and December 1946 the increase in bank deposits was £835 million.

Inflation Check

Moreover the coming of Sir Stafford Cripps, while it brought the policy of disinflation, did little to check the increase in the volume of money. Sir Stafford in his first year of office checked the inflationary expansion by a budget surplus; but one is forced to ask how much more flexible he might have made the economy had he not allowed the volume of bank deposits to increase by a further £266 million during 1948.

This laxity in monetary management was, to say the least of it, reprehensible. Nor is there any sign as yet that the Government is co-ordinating its policies. The rigid adherence to low interest rates, even after devaluation and in face of the fall in the prices of securities, indicates that no change need be looked for. The Chancellor in his Budget speech has admonished the local authorities for overspending.

How can he expect them to do otherwise as long as funds are available from the Public Works Loans Board at least a point lower than they are available to private business, either from the banks or on the issues market? Here surely is an inconsistency in Government policy. Further, it is an inconsistency which is not easily excusable, for State control of the Bank of England means that the reins of monetary as well as fiscal policy are now in the same hands. The responsibility falls entirely upon the Chancellor of the Exchequer.

Perhaps some faint hope may be drawn from the declining rate of increase in bank deposits and from the terms of the recent conversion of the $1\frac{3}{4}$ per cent. Exchequer Bonds. The rate at which the new Exchequer Stock was issued; the fact that the Government chose to repay by a new issue of medium-term stock rather than by additional Treasury Deposit Receipt borrowing; and the passivity of the Treasury in face of the decline in gilt-edged values, may all be construed by some people as signs that the tide of Ministerial opinion is on the turn.

Differing Policies

But one has only to set against these hopeful indications the Chancellor's refusal (reiterated in his Budget speech) to increase the lending rates of the Public Works Loans Board, and to bring short term rates up into line with the rates now prevailing in long- and medium-term securities, to realize how far monetary policy still is from agreement with general economic policy.

What should be the role of monetary policy if the main aim of economic policy, viz., full employment, is to be pursued by fiscal

means? Briefly the aims should be two: first to neutralize the effect of monetary forces and allow fiscal measures to work untrammelled; and second, to reinforce fiscal policy when it is insufficient or slow to act.

Reference has already been made to the first of these aims and to the way in which the Government has transgressed. Obviously if a policy of disinflation is being pursued by fiscal means it is rank folly to create such a supply of money as will encourage capital outlay and necessitate intricate and costly physical controls.

Situation Reversed

It would be no less ludicrous in the reverse situation to incur large budget deficits by public expenditure, while at the same time the banks restricted credit for private investment. The rate of interest can still act as a regulator of the level of private investment, and as such it should again be used, but it need hardly be said that its movements must be carefully timed and made to co-ordinate with changes in the level of Government outlay.

The public finance aspect of changes in the rate must also be considered in the light of prevailing conditions, but this should not normally be the governing factor. It must be remembered that there is no other means save that of arbitrary selection by a controlling authority of assessing the social utility of particular acts of investment. The rate of interest is qualitative as well as quantitative in its effect.

Both monetary and fiscal measures must work to the same end. The fact that the former works through the monetary supply, and the latter through the flow of incomes, makes it essential that the two should be continually co-ordinated. Even so, variations of the monetary supply may frequently have to be made in order to establish a particular rate of interest.

Here again it is essential that fiscal and monetary policy should be constantly in step. If the Government attempts to preserve a low interest rate at a time when a contractionary fiscal policy is under way (as at present) it is not only encouraging capital outlays by allowing the low rate, but it is creating a large and inflationary monetary supply to preserve it, and thus defeating its main policy.

Again the balance of argument appears to be in favour of (*a*) a more volatile interest rate, and (*b*) manipulation of the monetary supply to support the rate, and to back up the fiscal measures.

If we assign a more active role to monetary policy than that of neutralizing the effects of monetary forces, and regard it as assisting fiscal policy in regulating the tempo of the economy, then we must inquire as to the deficiencies of fiscal policy and to what extent monetary weapons can be used to offset these.

Courage Needed

The first and most serious drawback to which fiscal planning is inherently subject is that of timorous budgeting, due either to lack of knowledge or lack of courage. In the face of a serious recession only the most courageous measures will suffice. To embark upon isolated schemes of capital works will simply be to throw good money after bad. To this situation

monetary policy can render no assistance save that of low interest rates and easy credit conditions conducive to high private investment. The main attack must come from a widely conceived and carefully planned system of public outlays.

There is, however, one shortcoming of fiscal policy which monetary policy can help to eradicate. It is in the matter of timing. The action of purely fiscal measures may be slow. There is a time-lag between the making of primary outlays and the ultimate effect on incomes. For an expanding economy this time-lag is not serious, but when fiscal policy is used in the other direction, to check an excessive expansion, then slowness in action is a serious defect. Fiscal policy operates in the medium and long term rather than in the short term.

Here, it seems, may be a further use for monetary policy. The customary monetary techniques may serve as a short-term adjuster of the supply of funds, of liquidity and of the interest rate. For example, if it is desired to check expansion the check must act quickly. In such circumstances a sharp rise in the interest rate would be an effective means. This deterrent rate can be made effective by the central bank mopping up the surplus cash which might bid for existing securities and force the rate downward.

On the other hand during an expansion any selling pressure on securities, tending to raise the rate of interest and retard borrowing and investment, could be offset by an expansion of credit sufficient to meet the public's demand for liquidity. Used in this way monetary weapons would have a definite, albeit a secondary, utility.

Two Main Points

Two main points emerge: that monetary policy still has a role to play in the implementing of economic policy, and that the present Government have not availed themselves of it. The Government found it necessary, in order to secure the success of devaluation, to make still more strenuous efforts to control inflation and prevent the temporary advantage of devaluation from being dissipated in a rising spiral of costs and prices, and these efforts have been continued in the recent Budget.

Whether the specific measures taken are in themselves sufficient is debatable, but one thing is certain: unless the Government reinforces its fiscal policy and makes it an effective instrument, it runs grave risk, not only of failing now, but of bringing the use of fiscal weapons into disrepute and having them put aside for all time. That surely is not desirable.

FISHY

There are only two possible kinds of economic equilibrium in the North Sea fisheries. There is the sane balance of mutual restraint enabling a mere fraction of each country's present fleet to land a harvest ultimately bigger and in better condition than the present one, and to do so cheaply with a minimum of waste and danger. Failing this, free fishing will lead (if it has not done so already) to an uneasy oscillation between recurrent bankruptcies among fishermen and short-lived bouts of recovery among fishes, with consumers paying high prices for vessels to scrape corners of the North Sea for thin catches of undersized fish.

From the Economist, London, June 3, 1950.

Progress Report on Britain's Post-War Capital and Housing Problems

By PROFESSOR E. A. G. ROBINSON
(Cambridge)

WHAT progress has been made in overtaking arrears of maintenance and replacement of fixed capital and the replenishment of the depleted stocks of working capital?

At the end of the war it was estimated (see article* by Professor Paish in the *Bulletin* of February 10th, 1947: I have rounded some of his figures) that capital at home had been reduced to the extent of about £1,500 million by war damage on land and to shipping and to the extent of about £3,000 million by reductions of industrial and public utility capital in the forms both of fixed and working capital.

Both these figures are at the approximate costs of replacement of 1945/6. The figures do not, of course, include the loss of foreign assets, nor do they cover the very substantial reductions in domestic durable goods.

In very round figures, therefore, at prices of 1945/6, it would have required about £4,500 million to restore the volume of capital at home that the United Kingdom possessed in 1938. But in various senses that amount of net investment would not have left the country as well equipped as in 1938.

In the first place there has been growth of a little over 6 per cent. in the population. The exact capital needs to cover this cannot be accurately assessed from the information that is available; the population has changed in age composition as well as in numbers; certain services need not be increased proportionately with population; in some other respects we may be involved in a more than proportionate increase.

The total of capital assets at home in 1938 was of the order of £30,000 million at prices of 1945/6. It would have required something of the order of £1,800 million of net investment at those prices to cover the increases of population. In addition, the higher level of activity of our economy requires a greater volume of fixed and circulating capital.

There are now about $11\frac{1}{2}$ per cent. more men and women in civil employment than in 1938. The capital equipment of 1938 in some respects showed signs of being inadequate to the needs of the population of 1938, even at 1938 standards of capital per head. In 1937 the country manifested many of the signs of a boom despite an average of 10.6 per cent. of unemployment. There cannot have been a large margin of unused capital.

If we wish to estimate the cost of restoring the pre-war capital per head of those in civil employment we must add a further $5\frac{1}{2}$ per cent. of the capital assets devoted to in-

From British Economic Policy, 1945-1950, by E. A. G. Robinson assisted by A. D. Roy, London and Cambridge Economic Service, May, 1950.

* *Summarised in The Economic Digest, Vol. I., No. I., May, 1947.*

dustrial purposes (over half of the total of £30,000 million) beyond the 6 per cent. provision for the growth of population; this would amount to about a further £1,000 million.

The above calculations, which are inevitably no more than very rough approximations, may be summarised as follows:—

ESTIMATED COST OF RESTORING CAPITAL EQUIPMENT TO PRE-WAR LEVELS
(At prices of 1945/46)

		£ Mn.
(1)	Making Good War Damage ...	1,500
(2)	Arrears of Repairs, Maintenance and Replenishment of Stocks	3,000
(3)	Provision for Population Growth ...	1,800
(4)	Provision for Growth of Civil Employment beyond (3)	1,000
	Total of above	7,300

What inference can be made from these estimates? In very broad terms, we may say that the net investment made since the war will by the end of 1950 have done a little more than cover the war damage, the wartime arrears of maintenance and replacement, and the war-time depletions of stocks. At the present rate of investment, we shall not have made provision for the growth of population since 1938 until after the end of 1952 and we shall not, in the fuller sense described above, have restored the level of capital per head in industry and public utilities to its pre-war standard until sometime in 1954.

It is only thereafter that we shall begin to raise our pre-war standards of capital equipment generally.

Did This Inspire The Schuman Plan?

By GUNNAR MYRDAL*

In the interest of consumers and of the cost structure of European industry in general, it is highly desirable to maintain an effective international body, with the participation of importing countries, which can exercise some degree of oversight over the coal market. An effective Committee combining producers and importers, working within the framework of the United Nations, with the lack of secrecy guaranteed by that fact, and exercising a judicious influence on the market in the interest of stability, of improving productivity, and of maintaining the lowest possible economic level of prices, could contribute much to the economic welfare of all peoples.

In view of the history of the European steel industry, attempts to organize a new steel cartel are likely to develop, in the absence of international action undertaken to provide a more constructive solution for the pressures to which cartel organisations are often a response. I consider the development of an effective market policy to be an important problem which should be faced in the future by the Steel Committee. One step which might be contemplated is a special commodity agreement for the European steel industry.

The main purpose of such an agreement would be to widen the market, and to ensure fair and adequate competition for steel products among signatory countries. In such an agreement the governments might consider special provisions for market stability, at price levels which would promote consumption, while providing reasonable incentives for expansions in capacity, investment, and for reductions in cost.

**Executive Secretary, Economic Commission for Europe.*
Press Release, Geneva, April 19 1950.

Economics of Rent Restriction

by Professor F. W. PAISH
(University of London)

All parties admit that rent restriction has created intolerable anomalies and injustices. Professor Paish suggests remedies and a return to the Act of 1923 if the real remedies are politically impossible

PROFESSOR Paish begins by pointing out how little attention the economic aspects of Rent Restriction have attracted, considering their importance in the economic system. After sketching the history of Rent Restriction legislation he discusses the many legal difficulties, anomalies and injustices which result from the various Acts which have been passed since 1915.

" If the Rent Restriction Acts are a lawyer's nightmare," he writes, they offend at least as much against the ordinary standards of equity. Of three identical houses in the same road, one may be let at 10s. a week under the old control, the second at 15s. under the new control, while the rent of the third, let for the first-time since the War, may be 25s. or more.

" There is no guarantee that the poorest tenant rents the cheapest house, or the poorest landlord owns the dearest one. Indeed, the landlord of the cheapest house may well be poorer than his tenant, for before 1914 small house property was a favourite medium for the investment of small savings.

" But the inequity of the present system as between tenant and tenant, or between tenant and landlord, fades into insignificance as compared with the inequity as between those who are lucky enough to have rent-restricted houses and those who have no houses at all. It is an economic truism that the fixing of maximum prices without the imposition of rationing normally results in part of the demand at the fixed price going unsatisfied. Even if the maximum rents were completely consistent as between themselves this difficulty would remain.

" Since 1939, money earnings and most prices have approximately doubled; controlled rents (apart from increases in rates) have not risen at all. Thus, in real terms, the rents of some 8½ million houses out of the 13 millions of pre-war houses have been approximately halved.

Enormous Demand

" Is it to be wondered that the demand for houses to let at controlled rents is enormously in excess of the supply? Is it surprising that rent-restricted houses are used less economically than they would have been if rents had risen in proportion with other prices and incomes, and that an unsatisfied demand is squeezed out, to be concentrated on the other sectors of the market—local authorities' houses, furnished accommodation, and houses available for purchase with vacant possession?"

The two main economic disadvantages are the impairment of the

From Lloyds Bank Review, London, April, 1950.

landlord's ability and incentive to maintain premises in good condition and the impediments which the Acts place in the way of the mobility of labour. Professor Paish analyses the proposals for reform which have been put forward, notably those given in the P.E.P. publication of November 1949 (reviewed in *The Economic Digest* of January, 1950) and the suggestions made in Mr. Roy Harrod's book "Are These Hardships Necessary?"

Various suggestions have been made to deal with the problem of immobility. It might, for instance, be possible to make people more mobile by giving to anyone who surrendered the tenancy of a house priority for a new tenancy, whether in his own district or elsewhere. Such a measure, however, would encounter insuperable political difficulties; for to give a new-comer in the district priority over existing inhabitants, some of whom had waited perhaps for years, would reveal far too plainly the injustice of the present system towards those who are not lucky enough to have a house. No solution which does not make a serious attempt to deal with this injustice either has or ought to have any chance of acceptance.

Mr. Harrod's Plan

A similar objection can be made to the otherwise most valuable suggestions made by Mr: Roy Harrod in his book *Are These Hardships Necessary*? " Mr. Harrod suggests that the Acts should be repealed and rents be allowed to rise to their full market level, but that for a period of 10 years the landlord should be taxed the whole of the increase and the proceeds handed back to the tenant, who would receive them whether he stayed in that house or not. At the end of ten years, some readjustment of wages or taxes could be made, so as to avoid any transfer of income from the poor to the rich that the abolition of the old system might entail."

Serious Deficiencies

" While Mr. Harrod's scheme would do much to remedy the disadvantages of the present system, and would largely solve the problem of mobility, it has three serious deficiencies. The first of these is that it does nothing, for at least ten years, to make the landlord better able to provide for the increased cost of repairs; for the heavy tax would be just as efficient a promoter of slums as the present restriction on rents. Secondly, it perpetuates the random distribution of the subsidy between tenants, regardless of their means, so that a tenant with a larger income or smaller responsibilities might well receive a larger grant than one poorer or more burdened.

" Most serious of all is the difficulty that, while the injustice to the man without a house would in fact be somewhat reduced by making it possible for him to get one at the full market rent, Mr. Harrod's scheme would make the remaining inequity explicit and therefore less acceptable to public opinion than the even greater inequity implicit in the existing system.

" We have only to think of the feelings of a man who is on the point of getting a house, for which perhaps he has been waiting for years, at a controlled or subsidized rent, and who suddenly learns that

its rent has risen by fifty or a hundred per cent. He will receive no compensation for the rise in rent of a house he has never inhabitated, while his next-door neighbour, who got his house perhaps a month ago, will receive an allowance which is not only sufficient to cover the rise in his present rent but which he will retain in full if he moves into a cheaper house. The resentment against treatment so obviously unfair would certainly prevent Mr. Harrod's scheme from being put into force as it stands.

Fair Shares

" Any scheme, to be logically defensible, must endeavour to deal with the difficulties which Mr. Harrod's scheme ignores, as well as with those which it resolves. Landlords must be given a sufficient share of the increases in rent to enable them to maintain their premises in repair, and the benefits of the amounts collected in tax must be shared, not only by existing tenants, but also by those who are without permanent accommodation.

" To meet these points would involve two substantial departures from Harrod's scheme. In the first place, the landlord, instead of passing on the whole of the additional tax collected would be allowed to retain, say, 25 per cent. of the addition as provision for repairs, provided that the premises were in fact kept in a condition satisfactory to the local authorities.

" The second difference would be that, instead of using the proceeds of the tax to subsidize only existing tenants, the Treasury would use part of it to supplement incomes in accordance with need, by increasing children's allowances, old age and other pensions, and so forth, and the remainder to reduce the general level of taxation. They would thus increase all net incomes, but especially those of people least able to pay the increased rents.

" It might very well happen that the incomes of people with large families of children would be increased by more than the increase in the rents of their existing houses, so that they would be able to afford to move into the larger houses vacated by people without families now finding it advantageous to move into smaller ones.

" There is one further measure that would be needed to make this suggested scheme complete. Since all members of the population would benefit, in greater or less degree, from the increased allowances and reduced taxation, to impose the landlord's tax only on the owners of rented houses would mean subsidizing owner-occupiers at the expense of tenants. Owner-occupiers would, therefore, also have to be made liable for landlords' tax on their own houses to provide the means of financing the benefits which they, as a class, would receive from higher allowances and lower taxes.

Assessing Tax

" One of the major practical difficulties of the scheme would be to assess the tax on owner-occupiers in such a way that it would be both fair as between different owner-occupiers and would yield an amount sufficient to finance the benefits which they collectively would enjoy. This task of assessment would be considerably eased after 1953, on the completion of the re-assessment, on a more consistent

basis, of rateable values throughout the country.

Advantages

"The proposals here put forward seem on the whole to conform fairly well to the three criteria enunciated above—administrative convenience, equity as between persons and classes and economic desirability. To calculate the tax payable on a rented house only two factors would need to be known—the rent paid on the date on which the new regulations came into force and the rent paid in the current year. The whole of the elaborate legal framework of the existing Rent Restriction Acts would fall away.

"The economic advantages of the change would include not only the restoration of mobility but also an increase in the supply of the sizes of houses and flats most in demand. As people in houses too large for them tried to economize by moving into smaller premises, rents of the larger houses would fall relatively to those of the smaller ones.

"This would not only make it easier for people with large families to occupy the larger premises, but would make it more profitable to convert the larger houses, with relatively lower rents and therefore relatively lower landlords' taxes, into maisonettes or flats for small families. Thus, the number of dwellings available for letting would be increased at a fraction of the cost of building new houses. The tax on such converted premises would continue to be paid at the rate appropriate to the whole house before conversion.

"It must be emphasized that this scheme, if adopted at all, should be adopted as a whole. The omission of any part of it would destroy its balance, so that the introduction of the remainder might well serve merely to import new injustices in place of the old.

"If neither this scheme nor Mr. Harrod's is regarded as politically practicable, the simplest alternative would be to return to the methods of the Act of 1923. These would include some immediate increase in rent for landlords who kept their premises in adequate repair and the release from control of any premises which fell vacant. As a statutory tenancy can be inherited only once, it then should not take more than two generations to rid ourselves of the disastrous incubus of the Rent Restriction Acts."

EXTRACTION OF SILVER FROM INDIAN COINS

The Finance Minister of India has stated in Parliament that a special refinery, costing about 6,000,000 rupees, was being set up to extract silver from the quaternary silver coins, which were being replaced by nickel coins. There were about 600,000,000 ozs. of such alloy coins containing 300,000,0000 ozs. of silver. This included coins in circulation in Pakistan, recovery of which was governed by the formulas evolved at the time of the partition of India.

From : "The Hindu," April 2, 1950.

Rent Rebates Proposed Instead of House Subsidies

THE P.E.P. broadsheet " A New Policy for Housing Subsidies " summarises some of the facts stated and the conclusions reached in two earlier studies — " Rent Control Policy " and " Economics of the Council House "—which were reviewed in the January 1950 and April 1950 numbers of *The Economic Digest*. The third study outlines a new system which amounts to a change from a system of subsidies attached to houses to a system of rent rebates graduated according to need. Three possible methods of approach to the problem are described as follows: —

" The present payment to local authorities of a fixed subsidy per house might be continued, but the authorities could be asked to charge rents on the new principle; that is, rents based on the unsubsidised cost of the houses to those who could afford them, with rebates to those who could not. This procedure would have the obvious defect of accumulating surplus funds in districts where the level of earnings was high, while in areas of low earnings it might be impossible to finance rent rebates on the approved scale.

" The second method would involve a more drastic break with the past and for that reason may be considered less practicable and less desirable. All existing subsidies would be taken into a national pool, either at once or gradually, and redistributed to authorities as they needed them. This would involve repealing those sections of the various Housing Acts under which subsidies on pre-war houses were granted, which might be considered a breach of faith with local authorities. In any case, until the new system was working smoothly it would cause considerable dislocation in the revenue side of housing accounts. Under such a scheme local authorities would lose most of the responsibility for one of their major functions and would be left only with the details of its administration. For these reasons its introduction would almost certainly be resisted both by local authorities and by tenants.

Practical Method

" The third, and probably the most practical, method would be for all the existing subsidies to be paid, as before, to local authorities, but for no further subsidies to be given in respect of houses built in the future. The authorites would assess rents and give rebates as in the first method, and the central government would then share with them the burden of any overall deficit in the housing account, possibly in the same proportion as applies to present subsidies—one quarter local authority and three quarters central government. This would limit the proportion of the burden which the local authorities would have to bear, while at the same time it would discourage them from being too lavish. It would ensure that the subsidies were distributed in an effective manner, with

From " A New Policy for Housing Subsidies," P.E.P., London, April 24, 1950.

the least upset to local authority finance, and have the further merit of eliminating the financial inequality arising from the varying ratios of pre-war to post-war houses among different local authorities. The contribution of the central government could be made dependent upon the local authority complying, within limits, to a nationally determined scale of rent rebates."

A Fifteenth-Century Holding Company

The Story of the Medici Bank

By ARMANDO SAPAN

Monopolies are not a special feature of twentieth century capitalism. Five hundred years ago a branch of the Medici family began to extend their banking activities beyond their native city of Florence. By 1460 Cosimo de' Medici had partnerships in Venice, Rome, Milan, Bruges, London, Geneva and Avignon, and representatives of these firms dealt in almost all their markets in Europe and the East.

Thirty years later the bank was broken—brought low by political loans, slackening of branch discipline and the weakness of bi-metallism. There was also the unholy alliance with Pope Pius II which sought—and failed—to create a monopoly in alum.

THE branch of the Medici family known as that of Giovanni di Bicci (the ancestor of Cosimo, Piero and Lorenzo the Magnificent) were bankers, industrialists and *commerciants* of Florence who towards 1430 extended their activities beyond their native city. By 1460 Cosimo de' Medici had partnerships in Venice, Rome, Milan, Bruges, London, Geneva and Avignon. The firms' representatives transacted deals in almost all other markets in Europe and even in the East.

The Medici had three factories in Florence producing fine woollens and silks which were exported to the English, French, Burgundian and Papal Courts. They carried on an entrepot trade in wool from Britain, Flanders and the Near East, and in silverware, dyestuffs and foods such as spices, fruit and olive oil. They even imported tenors from Antwerp and Cambrai to sing in the Florentine churches, and dealt in art treasures from all parts of the Continent.

The rise of banking activity in Italy is traced to the closing of the old trading routes to the East when Asiatic xenophobia extended to the Near and Middle East. Vast capitals of commercial origin sought new uses. Some fed traditional industries and increasing military

Condensed by A. B. Chalkley from the Quarterly Review of the Banca Nazionale del Lavoro, January, 1950.

needs, and some flowed into banking channels, now swollen by the increased political activity of princes, who began to feel the need for loans on a large scale.

By 1469, Florence alone had over thirty large banks, headed by that of the Medici. The banking system consisted of four kinds of institution:

1. The banks giving short loans on security of personal property. As these charged usury, they were predominantly Jewish and required a licence from the Church, eventually restricting them to a maximum rate of interest of 15 per cent.

2. The "retail banks," which seem to have dealt in precious stones and gold, granting, but only rarely, loans on security of jewellery, and taking time-deposits at about 10 per cent. interest.

3. The "merchant banks," real deposit and transfer banks, acting also as money-changers.

4. The "big banks" (*banchi grossi*), combining trade and manufacture with exchange dealings.

Exchange Risk

The mediaeval bill of exchange was usually payable according to customary usuances—that between Italy and London was three months. The discounting of bills as done today was regarded as usurious, and therefore the bankers introduced an element of exchange risk by giving or receiving in return for bills other bills payable in a different place in a different currency; this ruse hid the stain anathematised by the ecclesiastical courts.

The Medici Bank was organised on holding company lines. The central bank and the branches were separate entities, but administrative control was exercised by the Florentine headquarters. This form grew out of the fact that the branches were capitalised by the Medici in partnership with other bankers, the former however holding the majority share.

The Medici alone directed policy, chose personnel, granted powers of attorney, and made decisions to wind up any bank. This close-knit structure was in contrast to the hitherto loose and multiform partnerships of earlier banking. Branch management was not entrusted to salaried managers but to local minority partners entitled to shares in the profits.

The capital of the banks was insignificant beside the turnover. The main operating funds came from time deposits requiring six months' to a year's notice of withdrawal. There is some doubt as to how interest was credited, as there is mention of a remuneration varying with profits, which would give these deposits more the nature of shares.

The credit instrument favoured by the Medici was the bill of exchange, and to record their extensive transactions in this medium a technique was evolved which is still used. "Nostro" accounts were opened for each client having two columns each side, the record being kept in both the local and foreign currencies; "Vostro" or "Loro" accounts were also opened and kept in the local currency only. The branch headquarters and inter-branch accounts were similar.

As a result of the decline of trading fairs during the fourteenth century, selling on commission became important and afforded the Bank another source of profit. It financed joint ventures with other merchants and evolved the technique of the joint venture account exactly in its modern form.

To the Medici, as to the mediaeval

bank generally, the yearly balance-sheet marked not merely a suitable point in the continuous existence of the business, but a technical dissolution of the "old" partnership and the inception of a "new" one. New books were opened, and although the "new" partners were usually the same persons, the "old" partnership was credited with balances due, which it was the "new" partnership's duty to "pay off" as transactions begun the previous year were completed. No alterations to the partnership articles could be made except at balancing time.

The Bank was at its zenith under Cosimo the Elder in about 1466; it declined under the magnificent Lorenzo, and came to an end in 1494. Between 1464 and 1466 two great ventures, daring but well-planned, were undertaken.

The first, in shipping, failed. Three galleys, built for an abortive Crusade, were bought up and converted into merchantmen. It was hoped that, based on Pisa, they would voyage profitably to and from Bruges, Rhodes and Constantinople, but results were disappointing. Florence's bid for shipping supremacy had to be postponed until much later.

Alum Enterprise

The second, their alum enterprise, was on a much larger scale. Alum, used both for softening wool and for fixing dye at a later stage of manufacture, came chiefly from the Middle East and was in the hands of the Genoese. But Turkish inroads shut off these supplies.

It was with exultation that Pope Pius II, himself of a banking family, announced the discovery of rich deposits on Papal lands near Civitavecchia. Exploitation of this local alum was to be accompanied by all the machinery of monopoly and output regulation, and to this end the Medici came to the help of the Papal Office.

The Medici Bank's Rome office acquired shares in the mining company which regulated output. The Pope was given royalties on production and two-thirds of the profits. The alum was sold through the widespread Medici branches.

Meanwhile all Christians were forbidden to buy alum from areas over-run by the infidel Turks, on pain of confiscation and excommunication. All Christian princes were "requested" to prevent imports of alum except that of the cartel.

Monopoly Threatened

The monopoly was soon threatened by the mines of the Neapolitan island of Ischia; but an agreement to share the market by fixing prices and outputs by quota and assigning selling-areas was made.

The dream of huge profits was dispelled by two facts. First, the monopoly was not complete; England, for one, remained outside. Therefore prices could effectively be raised above those ruling in neighbouring countries which imposed no restrictions as to the source of alum.

Second, what rises in prices were imposed encouraged contraband, and even the threat of ecclesiastical censure did not prevent Christians from accepting the cheaper, if Turkish, commodity.

This bold attempt was the forerunner of the sixteenth-century monopolies and rings like those of the Fuggers and the Merchant Adventurers. Further, it revealed

the lack of scruples shown by the Church in promoting monopoly, a violation of the principle of the *justum pretium.*

The cracks which began to appear in the structure of the Medici organisation had many causes. There were the excessive loans to sovereigns. Warning should have been taken of past loans, for many a banker had come to grief this way. But the fact that even long after the fall of the Medici, the Fuggers were still financing Charles V, leads us to believe that it is sometimes not possible, however advisable it may be, to avoid known dangers.

To carry out their economic policies, bankers needed the sovereigns' good-will; in exchange for permits of residence, of exploitation, of export and import, they gave the princes much-needed credit for their political policies. Again, the merchants of that time did not distinguish between political and economic ends, and often filled official positions of state in which the interests of both their private and their public business were unashamedly intermingled.

There is no doubt that the Medici were aware of the thin ice of princely credit. The partnership articles for the Bruges branch forbade loans to princes, lords, ecclesiastics or State officials. But in 1471 special permission came from Florence to lend up to £6,000 groat to Charles the Bold, and two years later this limit was completely removed. . . . Thus was the Trojan Horse introduced into the apparently impregnable Medici fortress.

But internal decay contributed too. The organisation became too unwieldy for the family headquarters to control. Lorenzo's penchant towards art and politics led him to relax the reins into the hands of the local branch managers. The overall vision, the driving centripetal and centrifugal forces, weakened.

A further cause was the rise in the value of the internationally acceptable gold florin as the silver currency was debased and devalued. Profits on transactions fell, heavy losses were sustained on remittances, and liabilities increased as deposits rose in value. The only way out, a reduction in interest rates, was one which, the Medici feared, would adversely affect their credit. Not until no interest was possible was the desperate situation revealed.

To sum up: political loans, a slackening of branch discipline and the weakness of bi-metallism brought the Bank low. The Bruges, Lyons and London branches failed towards 1478.

Meanwhile the founding family occupied itself with the more amusing business of collecting works of art and acting Maecenas to Florentine writers and painters. Such pursuits are always expensive; soon the banking vaults were drawn on. The magnificence of Lorenzo was patrimonial prodigality. The inherent stability and funded strength of the organisation are proved by the fact that not until 1494 did the Bank finally crumble. In that year Piero di Lorenzo was driven out of Florence and the Medici estate was sequestrated. The undertakings of the family were found to consist chiefly of deficits, the worst being that of the Rome branch, where the net liabilities amounted to 11,243 florins.

Outlook for Israel

by Dr. A. HILDESCHEINER

Israel is an experiment in nation-buildng on a scale and at a tempo seldom attempted before in history

THE population of Israel has now reached the magic figure of one million Jews. Nearly 350,000 newcomers have entered the country since the foundation of the state. Nearly 30 per cent. of them are from Poland, 17 per cent. from Bulgaria of which the Jewish population has emigrated in its entirety, 14 per cent. from Rumania, 15 per cent. from the Arab countries of North Africa, Yemen, and Aden, 10 per cent. from Central Europe (Czechoslovakia, Hungary, Germany, Austria), and 8 per cent. from Turkey.

The moulding of this disparate human material into a homogeneous nation is the great task which Israel has undertaken. For emotional and ethical reasons the doors have been held wide open for the sick and the aged. Many of the newcomers are tubercular or suffering from malnutrition. Some of them are mentally sick or incurable. Hospitals are overcrowded. Housing is inadequate and more than 80,000 newcomers are living in wooden huts or under canvas. Tens of thousands of others are trying to turn the primitive shelter of abandoned Arab villages into homes.

Reduced to its simplest terms Israel is endeavouring to double its population within the next five years. It is as though the United Kingdom were to open its doors to ten million immigrants a year or the United States to thirty million.

In addition to one million Jews, Israel's borders contain 150,000 Arabs, and smaller minorities of Druze and Circassians. The rights of non-Jewish inhabitants are protected. They are citizens of Israel. Arab representatives sit in the Knesset, the parliament of Israel, and speak freely in defence of their own people's interests.

It is a tiny country among the geographical giants of Asia. Its azea is less than 20,000 square miles In mandate days the size of Palestine used to be compared with Wales. It was half the area of the latter country. Israel is even smaller, because Samaria and parts of Judæa are under Arab control.

Waste Spaces

The new immigrants are so far occupants of the land. It remains to be settled permanently. Camp life is wasteful and contributes nothing to national development, and the cultivation of the waste spaces is among the most immediate needs of the country. Galilee is almost empty. The Negev, the great southern waste-land, is unpopulated.

Both the government of Israel and the Jewish Agency, which is responsible for the immigration and settlement of Jews in Israel, are striving to divert as many new

From Progress, Lever Brothers and Unilever Ltd., London, Spring, 1950.

families as possible away from cramped cities and crowded villages into the empty land area. At the same time plans are afoot to extend the cultivable land area by irrigation where rainfall is inadequate, by terracing to halt the age-old process of erosion, and by afforestation to restore the physical and chemical properties of a soil which has been exhausted and neglected for hundreds of years.

The Kibbutz

Although agriculture must for some considerable time to come form the most important sector of the country's economy, only a small proportion of the needs of the national larder is satisfied by local products or manufactures. There is, however, a growing force of experienced farmers, skilled labourers, and agricultural technicians to train newcomers to the land. The social forms of agricultural organisation, in particular the *kibbutz* or collective settlement, provide ready means of practical education in farming for many immigrants who are prepared to pioneer.

Most of the settlements are co-operative in structure. Agricultural wages in Israel are among the highest in the world. For purposes of rapid expansion mechanical implements are essential. The number of tractors, combines, and other agricultural machines in use in Israel compares very favourably with other sub-tropical areas, and is higher than anywhere else in the Middle East. In addition the most scientific methods of soil irrigation are practised, while experiments in selection, breeding, and hybridization have produced new types of plants, cattle and poultry specially adapted for successful development in the climate of Israel.

Israel's most valuable agricultural product is citrus fruits, marketed either in the natural state or in processed form throughout the world, chiefly to Britain. But there are also bananas, grown successfully in the tropical Jordan valley settlements, melons, marrows, egg-plants, and a host of other vegetables. Dairy farming and poultry raising are also flourishing industries.

Figures of recent expansion reveal the stimulus given to agricultural development by the foundation of the new state. In the past eighteen months 130 new settlements have been established, 50 of them by new immigrants. This compares more than favourably with the total of 257 settlements in existence at the outbreak of the second world war.

Industrial Progress

Industrial progress has been considerably assisted by the experimental work of a number of scientific research institutes, of which the most important is the Weizmann Institute at Rehovot. Other research groups are at work at the Haifa Technical School and the Hebrew University in Jerusalem. The government has also established a national scientific council for further development projects.

Israel's economic planners realise that their country's natural resources are limited. They are endeavouring to supplement them by the development of highly productive skills and crafts. Another small country, Switzerland, is the example they most frequently quote.

Among earlier and more recent immigrants into Israel are large

numbers of skilled craftsmen in a vast variety of industries which depend on precision work. Some of them have helped to establish small industries in the *kibbutzim*, including carpentry, textiles, motor accessories, and hundreds of other lines. The requirements of British forces in the Middle East during the war were a great stimulus to production.

Industrial Experts

Industrial experts and technicians settled in Israel as a result of the persecution of the Jews in Central Europe. Among them is the former director of the German Zeiss-Ikon factories, who has trained new cadres for Israel's optical industry. There are also a number of chemists who gained their experience with the I.G. Farben group, and have now set up a growing pharmaceutical industry which has already begun to export.

Textile mills have been set up by manufacturers from Czechoslovakia and Germany. And Unilever experts have launched the margarine industry in Israel.
strange, but highly specialized products of Israel's industry are false teeth, which have found a substantial market abroad.

Israel is not rich in natural resources, but a large number of minerals and raw materials are available in commercial quantities. The Dead Sea, of which Israel controls the southern end, is the source for potassium chloride, magnesium chloride, sodium chloride, magnesium bromide, and many other minerals. Other minerals found in Israel include rock salt, gypsum, manganese, kaolin, bituminous limestone, and asphalt. Traces of oil have been discovered in various parts of the country, and geologists are examining the possibilities of boring.

Israel has an abundance of raw materials for building and road construction. There is a large Portland cement works at Haifa which makes use of native chalk. But its share in the Dead Sea is Israel's largest mineral asset, and so far only its surface wealth has been tapped. Its content of potassium salts has been estimated at upwards of 2,000 million tons, which could be refined more cheaply here than anywhere else in the world.

Limitless markets are at hand in the impoverished soil of Asia and Africa, but for their development more settled political and economic conditions will be needed. There are also 5,800 million tons of magnesium in the Dead Sea, which could be the essential raw material for light-metals industries. At Haifa a large plant is in operation drawing for its supplies on the waste by-products of the giant refinery near the port.

Oil Refineries

When disputes over the future of the Haifa refineries have been resolved, they may play a leading part in Israel's growth as an industrial power. Haifa could handle four million tons of refined petroleum products a year, which would help keep going the country's industry, agriculture and transport.

The enormous influx of new immigrants has created a steadily increasing home market for a whole range of products. Housing is a primary need. The government has encouraged the construction of large numbers of temporary dwellings and is importing pre-fabs of all types. Simultaneously, new building schemes for permanent housing

have been launched which will include the development of new suburbs for existing cities and complete new towns in various parts of the country.

Full Employment

The building trades are likely to be an important factor in the maintenance of full employment in Israel for years to come. Cement, stone, steel, glass, wood, and a host of other industries will continue to employ thousands of workers, and manufacturers of domestic equipment and appliances will employ thousands more. The largest cement factory in the country, that of the Nesher Company at Haifa, is turning out 500,000 tons of cement a year. The Phoenicia glass-works is working on a three-shift basis.

Citrus, Israel's staple product, has met with some difficulties in the export market, but the government is assisting growers with loans and subsidies, and efforts are being made to negotiate wage agreements which will give the industry a chance to meet foreign competition. Diamond-cutting, which received great stimulus during the war as a result of the German occupation of Holland and Belgium, has had some setbacks, but the basis of a highly profitable industry has been established.

New factories are under construction to satisfy home needs. They will produce electric light bulbs, piping, refrigerators, and a vast number of other products. The Government - controlled railway shops are busy making new passenger carriages and goods trucks for the Israel State Railways, which are once again in operation. Shipyards are to be built, as well as assembly plants for motor vehicles, cold storage plants, and silos.

The improvement and extension of the country's transport system are necessary prerequisites for the development of industry. The rail and road transport facilities need co-ordination and improvement, as do the postal and telephone services. The expanding tourist trade will make further heavy demands on transport and communications. The government is actively interested in shipping and air transport. Lydda is once again an important international airport.

The government is faced with heavy financial responsibilities. It has to establish the country's economic life on a sound footing. At present Israel has a heavy adverse balance of payments. The cost of living is extremely high, although heroic efforts have been made with some success to hold prices in line, and in some cases to reduce them. A wide variety of industrial and commercial expansion has been undertaken by government, the municipalities, co-operatives, and private investors both in Israel and abroad. The need is for their co-ordination.

The current budget is divided into two parts. The first provides for the raising of I£40 million by heavy taxation. There is also an extraordinary budget of I£55 million for development purposes, which will be covered by domestic and foreign loans, including that of 100 million dollars from the American Import-Export Bank, gifts from Jews abroad, private investment, and capital brought into the country by new immigrants.

For years to come Israel will be faced by the need to improve its balance of payments by restriction of imports and expansion of exports.

DIGEST Book Review

Economics of Everyday Life

By GERTRUDE WILLIAMS

THIS book* is of unusual interest and importance. Mrs. Williams faces the question why so few people think that economics is of any concern to them and why so many regard the subject as altogether beyond them or mistrust economic theories because so many have proved to be wrong and because economists cannot agree among themselves which theories are right.

The sort of questions the average person might be expected to ask are set out in the Introduction:

"Need we be poor? Are we producing as efficiently as we could? and, if not, why not? and how could we do better? Are we producing the 'right' things? What are the 'right' things? Who ought to decide this and why? Is specialization always a 'good' method of production? and in what sense, 'good'? Might we become too dependent on foreign supplies and does this matter?

"Is it better to buy goods produced in your own country? 'Better' in what sense? Does it make one richer? or safer or what? Is monopoly better than competition? always? sometimes? in what circumstances? Why does a miner usually earn less than a doctor? and what would happen if you insisted that they should get the same amount? Why does the Government settle some prices and not others? and who settles the price if the Government doesn't?

"These are the sort of questions that a study of economics helps us to answer, and they are the kind of questions which underlie the issues on which the ordinary citizen votes at elections. If a motor car breaks down nobody but a fool expects to be able to repair it without some elementary understanding of the mechanism, and the economic system is a good deal more dangerous to tinker with than a car. Unfortunately it is also much more difficult to understand, and there are two main reasons for this.

"1. The various bits and pieces of a car are identical in all the cars of one pattern, and you know exactly how each bit works in relation to the others. But the bits of the economic system are human beings who are not identical and whose actions cannot be precisely calculated or foretold.

"2. More important than this variability of human actions is the fact that you cannot separate people's economic activities from the remainder of their lives, and that all sorts of things which are not primarily economic influence the way in which men and women behave in earning and spending their incomes.

"We are not robots, and there is

*Economics of Everyday Life, by Gertrude Williams, Penguin Books, June, 1950.

no such thing as an economic man. We all live in social groups, and the things we value or despise, the kinds of behaviour that we extol or condemn, or simply take for granted as natural, and the ends for which we are ready to make sacrifices, are all products of our cultural codes of behaviour.

Social Forces

"From our earliest moments we are shaped by the social forces in which we live—even as babies we are kissed for one kind of behaviour and scolded for another—so that by the time we begin to take a place in the wider social groupings, at school, at work, or in the outside world, we have come to respond to certain stimuli and reject others. Our scales of value are not individual ones; they are the personal variations we make on the social evaluations fixed by the community in which we have grown up. . . .

"These two points are worth stressing because it is necessary to realise that economics is a study of a living and working society and not a blue-print for an ideal community. The aim is not to find out how people ought to behave in different circumstances but how, in fact, they do behave in the circumstances in which they live.

"By patient observation we try to discover if there are ways of reacting which are so general that we can use them as guides in our attempts to prognosticate the future, and it is to these generalisations, based on observed facts of human behaviour, that we give the name 'economic law.'

"Such laws are not, therefore, in the same category as the laws of chemistry or of natural science; we cannot say that, given such and such circumstances, such a result is bound to ensue; all we can say is that it is likely to ensue with the proviso, either implied or explicit, that there may be—will be—innumerable exceptions to the general rule.

"It is, indeed, for example, true in a general sense that the majority of people in an industrial country such as England are eager to get as good a money return for their work as they can, so that a rise in wages in one industry may be expected to draw larger supplies of workers into it and a fall to cause many workers to withdraw and find other jobs.

"By and large, and given time for changes in wage rates to become widely known, this is true; but it does not mean that every person always goes to the job that pays best in this way. A man may be attached to a particular kind of work, or to the firm that has employed him for some time, or may not want to move from the locality where his friends and family live, or may prefer country life to urban (or the other way round) or may prefer the 'amenities' that go with one type of work, such as higher social prestige, or greater freedom, or what have you.

Society's Influence

"In a society in which the material equipment of well-being (good furniture, good clothes, the frig. in the kitchen, etc.) is given the highest place in social evaluations, changes in wage rates are likely to have a much more direct influence on supplies of labour than in one in which all these other factors play a bigger part. What adds to the difficulty is that the pattern of behaviour is not a static thing—fixed

once and for all—but is continually being modified by new circumstances and ideas, and one must be forever on the alert not to assume that the series of economic reactions observed in the past will inevitably repeat itself without modification in the future.

"There is no doubt, for example, that during the present century both security and leisure have come to play a much bigger part in the economic calculations of the wage-earner than they did in his father's time, and this must be taken into account both in the attempt to explain what has happened in the occupational distribution of the population and in the efforts we make to alter it if we think this necessary."

The succeeding chapters explain economic problems in simple language from the international, national and individual standpoints. The longest chapter "Incomes and How we get them" is, perhaps, of most general interest; all alike are equally well written.

Shorter Book Notices

MEMORANDA PRESENTED TO THE ROYAL COMMISSION ON POPULATION
(*H.M. Stationery Office*, 3/-.)

Almost exactly half of this publication is of first-grade economic interest. The economic position of the family is discussed by Mr. J. Hajnal and Professor A. M. Henderson. Mr. Roy Harrod—in the course of a memorandum, a plan with necessary tables, and a supplementary submission—presents what is likely to become the classic case for family allowances rising with the parents' incomes. The aim, of course, is to encourage a higher birth-rate in those sections of society where quality of children is on average the highest. The task is obviously important, and Mr. Harrod faces squarely the technical difficulties. At some future time it may need all Mr. Harrod's skill as a politician to put over his expert ideas as an economist. All thoughtful people will be grateful to him. The other section of the publication deals with relations between intelligence and fertility. Professor Sir Godfrey H. Thomson wrote the original memorandum, and a final commentary after evidence from several other distinguished scientists.

ECONOMIC DEVELOPMENT IN SELECTED COUNTRIES Vol.II
(*United Nations. Lake Success, February* 1949)

This report, the second study dealing with the development programmes of individual countries (the first was issued in October, 1947) outlines programmes in Australia, Bulgaria, Columbia, New Zealand, the Philippines. Puerto Rico, Southern Rhodesia and the Union of South Africa. As the individual data are normally not readily available, the volume is an indispensable reference book for all interested in the problems of economical developments.

MINING JOURNAL ANNUAL REVIEW, 1950.
(*Mining Journal*, 5/-.)

This annual review, surveying the year 1949, is the more valuable because no similarly complete survey of mining events and statistics has been possible for ten years. It runs to 200 pages, contains seventy articles and all relevant statistics, and covers the world. It deserves in future to appear as a bound book, since it is an indispensable reference work in its special field.

Worth Reading—

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Distribution of the Proceeds of Industry. *Ditto.* (Both studies are concerned with Australia).
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The Telephone Service. *Westminster Bank Review, London, May*, 1950.
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The Statistical Approach. M. G. KENDALL, *Economica, London, May*, 1950. (Non-technical in style, entertaining, but profoundly critical).
Distribution of Incomes in U.K. 1938-1947. E. C. RHODES, *ditto*
Present Pattern of Government Control of Industry. *National Provincial Bank Review, London, May*, 1950. (Useful appendix to article by H. G. HODDER on Government and Industry).
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Wage Incentive Schemes. *Personnel Management Series* 3, *British Institute of Management, London, March*, 1950.
Organizing for Output. *British Institute of Management, London, April*, 1950.
Immigration and the Labour Shortage. R. J. CAMERON, *Australian Quarterly, Sydney, March*, 1950.
Business Conditions Across Canada. *Monthly Review, Bank of Nova Scotia, Toronto, April*, 1950.
A Stable and Expanding World Economy. G. D. N. WORSWICK, *District Bank Review, Manchester, June*, 1950.
The Economic Integration of Europe. *Ditto.*
International Finance. G. S. DORRANCE, *London and Cambridge Economic Service, May*, 1950. (The Sterling Area now shows a net surplus on its dollar transactions, the result—it would appear—of increased dollar earnings by the rest of the Sterling Area rather than by U.K.).